Threats to Security, Threats to Economy

The Real Risks in the Reaction to the Sale of U.S. Terminal Operations to a Dubai Company Are Alienating Our Allies and Disrupting the Flow of Capital at a Critical Time in Our Economic History

Testimony of
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Hearing on
"Foreign Investment, Job, and National Security: The CFIUS Process"

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Mme. Chair, members of the Subcommittee:

It is an honor to appear before you as a witness today for this important hearing on "Foreign Investment, Jobs, and National Security: The CFIUS Process."

My name is James K. Glassman. I am a resident fellow at the American Enterprise Institute, where I specialize in matters of financial and economic policy. I am also host of TCSDaily.com, an international online journal that focuses on technology, economic and public policy. In addition, I am chairman of Investors Action Alliance, an organization that educates small investors and stands up for their interests.

The feverish reaction of much of the media and many public officials to the imminent transfer of shipping-terminal operations at six U.S. ports raises disturbing questions about national-security priorities and about America's commitment to her staunchest allies and to the process of globalization.

At the heart of this reaction is a frightening specter: a dirty radioactive bomb or a full-fledged nuclear device shipped into a major city in one of the nine million trailer-sized containers that enter U.S. ports annually.

The fear of such an attack is a real concern, but the notion that a sale of assets to a Dubai company will increase the threat of such an attack is, emphatically, not.

The recent uproar is puzzling in that it does not appear to fit the facts. For example, one member of the U.S. House wrote President Bush:

"In regards to selling American ports to the United Arab Emirates, not just NO – but HELL NO!"[1]

Actually, no American ports will be sold to the United Arab Emirates. The ports are owned by state and local authorities. A company called Dubai Ports World, based in the United Arab Emirates and currently doing business in such nations as Germany, Australia and the Dominican Republic, will, if the deal is fully consummated, take over terminal operations – the loading and unloading of trailer-sized containers – currently conducted by Peninsula & Oriental Steam Navigation Co., based in London.

In another example, a U.S. Senator stated:

"Why in the world should we let this rogue government control ports in the United States?"[2]

[1] Rep. Sue Myrick, letter to the Hon. George W. Bush, Feb. 22, 2006.

But the United Arab Emirates, formed in 1972 by seven small Persian Gulf states, is not a “rogue government.” It is a nation of 2.6 million people with, according to the CIA Factbook, “an open economy with a high per capita income.” The United States government has had close and friendly relations with the UAE, especially since the attacks of Sept. 11, 2001. Indeed, the UAE has been a model citizen in the region, recently entering into an important trade agreement.

Gen. Peter Pace, chairman of the Joint Chiefs of Staff, says that the U.S. has a “superb” military relationship with the UAE. “In everything that we have asked and worked with them on [including providing a base for U-2 spy planes and unmanned surveillance aircraft for fighting in Iraq and Afghanistan], they have proven to be very, very solid partners.” It’s doubtful that the U.S. would have sold 80 of the most sophisticated versions of the F-16 fighter jet to a “rogue government.”

As a final example, another member of the U.S. House stated:

“Recently, the Bush Administration approved the takeover of six United States ports’ security by Dubai Ports World…. The Bush Administration has been outsourcing jobs for five years, and now they want to outsource our national security.”[3]

In reality, primary responsibility for port security in the United States lies with the U.S. Coast Guard, the U.S. Customs, and Border Protection officials. In addition, most ports have their own law-enforcement authorities as well as local police. DP World also has responsibility for security, but its record globally indicates no more cause for concern than there would be with any other terminal operator – probably less.

As my colleague at the American Enterprise Institute, Veronique DeRugy, has written: “Foreign operation of American ports is nothing new. At least 30 percent of terminals at major U.S. ports are operated by foreign governments and businesses…. Ownership does not affect in any substantive way the dynamics of terrorist infiltration.” Shipping security experts know that what is crucial is preventing nuclear material from being placed on vessels in foreign ports in the first place.

Recommendations

Fact-based or not, the criticism led, on Feb. 26, to a decision by DP World to request a 45-day re-examination of the American portion of its transaction.

In my view, the response to the DP World-P&O deal is wholly out of proportion to the possible risk involved. It has damaged our relations not just with the UAE but with Arabs and Muslims and others disposed to support American policies and values. That damage could hurt our overall national security efforts.

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[2] Sen. Frank Lautenberg, press release, “Lawmakers Begin Push for Thorough Federal Review of United Arab Emirates-Owned Company Taking Control of Major U.S. Ports in NY, NJ and East Coast,” Feb. 16, 2006.

[3] Rep. Sherrod Brown, Feb. 24, 2006, www.huffingtonpost.com.

Perhaps worst of all, the near-hysteria threatens to disrupt capital flows to the United States at a time when those flows are desperately needed.

I urge this subcommittee and the Congress to use put this episode to positive use in the following way:

1. Re-examine and, if necessary, change the process of approving strategic foreign purchases of assets in the United States so that the process can enjoy a high level of public confidence and congressional respect.

2. Assess the true nature of the terrorist threat as it involves shipping. That threat has little to do with the unloading of container vessels in U.S. ports and practically everything to do with the loading of such vessels in foreign ports.

3**. Re-assert this nation's commitment** to the free flow of trade in all its manifestations: goods, services, and investment.

4. Repudiate any semblance of racial and religious bigotry. As President Bush said in connection with this sale: "What I find interesting is that it's okay for a British company to manage some ports, but not okay for a company from a country that is a valuable ally in the war on terror."

Background

The Sale of P&O

Tomorrow, March 2, Dubai Ports World is scheduled to complete its purchase of Peninsula & Oriental Steam Navigation Co., the venerable shipping firm, founded in 1837, based in Pall Mall, London, and long associated with the eastern reaches of the British Empire, celebrated in the works of Rudyard Kipling and Somerset Maugham.

Over the past century, P&O evolved from the largest global steamship company to a firm whose main business is operating container terminals – 29 of them around the world, handling the equivalent of 22 million 20-foot-long trailer-loads of goods a year and ranking fourth in the world, with a 6 percent market share.

Six of P&O's terminal operations are in the United States, in areas leased from public port authorities in Philadelphia, New Orleans, New York, Newark, Miami, and Baltimore. Typically, P&O is only one of the operators in such ports. Such an operator has a landlord-tenant relationship with the actual port owner, usually a public authority. In New Orleans, for instance, P&O leases about one-fifth of the loading area.

DP World, the world's six-largest terminal operator, prevailed in a bidding war for P&O with Temasek Holdings, the Singapore government's holding company, which controls the number-two terminal firm. DP World is also a state-controlled entity, owned by the ruler of Dubai, Sheikh Mohammed bin Rashid al-Maktoum.

The Committee on Foreign Investment in the United States (CFIUS) -- comprising representatives of the departments of the Treasury, State, Defense, Homeland Security, Commerce, the Attorney General and other U.S. agencies -- reviewed and, on Jan. 23, approved the acquisition of the six American terminal operations by DP World. According to published reports, U.S. intelligence agencies also supported the transaction,[4] and, as part of the process, DP World agreed to additional security measures. "What had been voluntary is now a mandatory program," said Stewart Baker, an assistant secretary at the Department of Homeland Security. "There are more safeguards in this transaction than in any past port" deal.

In mid-February, members of Congress of both parties and local officials in the states involved began objecting heatedly to the transfer of assets. One governor called the sale a threat to both state and "national sovereignty."[5]

Critics in Congress introduced legislation to delay or prohibit the sale. On Feb. 26, DP World responded by requesting a 45-day re-examination of its deal. Meanwhile, the company agreed to separate the six U.S. terminal operations from the rest of its purchase, and P&O's North American-based executives would continue to run port operations after DP World formally takes control of P&O tomorrow. Some members are proposing as well that Congress have 30 days after the re-examination to give final approval to the transaction.[6]

Dubai Ports World

After the sale, Dubai Ports World will become the second-largest terminal operator in the world. Currently, DP World operates container terminals in Germany, South Korea, Australia, Malaysia, Hong Kong, China, India, Romania, the Dominican Republic and other countries.

DP World's sister company, the Dubai Ports Authority, also operates ports in the UAE. These ports, which can accommodate aircraft carriers, are being extensively used by the U.S. Navy.

DP World, according to Business Week, is "a well-respected company with global reach." Just last week, DP World was named "container terminal operator of the year," by Lloyd's List, the shipping newspaper.

In 2004, DB World bought the operations of Jacksonville, Fla.-based CSX Corp. for $1.2 billion. (None of those terminals is in the United States.) DP World is paying $6.8 billion for P&O, with about half the funds raised in a convertible bond issue in January. Several of the company's top officials are American. They include DP World's chief operating officer, Ted Bilkey, who was previously vice president of the largest container terminal operator in the New York area; senior

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[4] "U.S. Intelligence Agencies Backed Dubai Port Deal," Washington Post, Feb. 25, 2006. The Post said that "the intelligence studies were coordinated by the Intelligence Community Acquisition Risk Center, a new organization under the office of the Director of National Intelligence."

[5] Gov. Jon Corzine of New Jersey.

[6] This week, it was broadly reported that the Coast Guard raised concerns that, because of U.S. intelligence gaps, it could not determine whether DP World might support terrorist operations. This story produced lurid headlines. The very last paragraph of the Associated Press report, however, read: "In a statement, the Coast Guard said the assessment was part of a broader classified Coast Guard analysis that concluded that DP World's pending takeover 'in and of itself, does not pose a significant threat to U.S. assets in [continental United States] ports." AP, at www.Forbes.com, Feb. 28, 2006.

vice president Michael Moore; and Dave Sanborn, who was nominated in January by President Bush to be U.S. Maritime Administrator. DP World's chairman, Sultan Ahmed bin Sulayem, is American-educated. Currently, P&O employs only 430 workers in the United States – all or nearly all of them American. Another 6,000 longshoremen are hired on a daily basis. Those hiring practices are not expected to alter with DP World's purchase.

"In practical terms, nothing is going to change at U.S. ports in day-to-day operations," said Tim Power of Drewry Shipping Consultants. "DP World's taking over P&O does not mean a lot of people are suddenly going from Dubai to the U.S. to manage the ports."

U.S. ports in recent years have grown outdated, and the best technology – and most activity – has moved elsewhere, especially to Asia. DP World may be the best thing to happen to the American shipping scene in decades. It has a track record of spending money to make money and of bringing in top management talent.

United Arab Emirates

Prior to the attacks of 9/11, the UAE was one of only three governments (the others were Pakistan and Saudi Arabia) that recognized the Taliban in Afghanistan. After the attacks, all three countries immediately cut their ties. The UAE was home to two of the 9/11 hijackers, and the FBI has said that the UAE banking system was used to transfer funds to the hijackers. In addition, according to The Economist, "A.Q. Khan's Pakistani nuclear-smuggling network…was hidden behind a Dubai front."

In the past four and a half years, however, since the war on terror began, the UAE has been a staunch U.S. ally, providing "significant assistance both in passing along terrorism tips and in helping to apprehend suspects."[7]

The UAE has provided services for 700 U.S. Navy ships a year at its ports, including the DP World-operated terminal of Jebel Ali. In fact, the UAE hosts more U.S. Navy visits than any port outside the United States, and Dubai is a popular port for sailors on leave. As former secretary of the Navy Will Ball recently wrote on TCSDaily.com: "In a region of the world not previously known for "liberty ports" that compete with their Mediterranean and Western Pacific counterparts, the new Dubai is fine, fine indeed, according to the sailors of today. Harbormasters, citizens and yes, even port security officials there afford an especially warm welcome to American warships -- aircraft carriers in particular."

DP World is also the primary support contractor for U.S. Air Force assets at Al Dhafra Air Base, where refueling and reconnaissance flights originate for southwest Asia.

Economic Implications

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[7] "Bush and Congress Clash Over Dubai Ports Deal," Wall Street Journal, Feb. 23, 2006. The terrorists apprehended "were not small fries," said a former U.S. ambassador to the UAE.

By any objective analysis, the United Arab Emirates has embraced the security and economic prescriptions of the United States. “Dubai,” says a news article in the Feb. 26 edition of the Financial Times, “has gone out of its way to project an image as a pragmatic, pro-Western and free-market exception in a region often bristling with hostility to America.”

Al-Maktoum, Dubai’s ruler, not only has developed Jebel Ali into a huge free port, one of the largest in the world. He has also created one of the world’s largest airlines, Emirates, and launched what Business Week calls “a new financial center that is attracting the cream of the world’s banks.”

At the very least, the reaction to the purchase of P&O has similarly pro-Western business leaders in the Arab and Muslim world scratching their heads in bewilderment and wondering whether racial prejudice, misinformation or paranoia is behind the hysteria.

One could argue that the UAE is at least as strong an ally of the U.S. in the war on terror as France. Yet a French company, Suez, owns plants in 17 states that provide seven million Americans with drinking water daily. An article in Lloyd’s List, the shipping newspaper, noted: “Venezuela’s Hugo Chavez, whose opinions about President George W. Bush and Secretary of State Condoleezza Rice would make a lesser man and woman blush, controls Citgo, and its terminal and refinery in Philadelphia.” While it’s true that two 9/11 terrorists came from the UAE, it’s also true that the man who attempted to set off a shoe bomb on a transatlantic flight was a British citizen, and several U.S. citizens have been arrested as terrorist suspects as well.

Meanwhile, DP World’s purchase of terminal operations in Germany and Australia – countries that have concerns about terrorism similar to those in the United States (more Australian civilians have been killed by terrorists since 9/11 than American civilians) – produced no notice at all.[8] “I can’t really see the security question coming up as DP World is a well established, respectable company,” said Patrick Verhoeven, secretary general of the European Sea Ports Organization.

The over-reaction of many public officials in the United States to the terminal transactions, coupled with Congress’s recent thwarting of the purchase of Unocal by a Chinese company, cannot help but deter other investments, especially by developing nations, in this country.[9] “Xenophobia,” as The Economist put it, “seems to be creeping into American politics.”

The arithmetic of foreign investment is not complicated. The current account deficit has been rising for the past decade and now is 6 percent of GDP, indicating a wide gap between what we buy, in goods and services, from foreigners and what we sell to them. This deficit has not harmed the U.S. economy for a simple reason: the United States remains one of the best places in

[8] To take the flawed logic of the critics further, Ivan Eland of the Independent Institute wrote, tongue in cheek, on Feb. 20, 2006: “Perhaps even airlines from Arab countries should be banned from landing at U.S. airports because they might be used in terrorism or bring terrorists to the United States – in spite of the fact that the planes used on 9/11 were all U.S. airliners.” (www.independent.org)

[9] As a news story in The Wall Street Journal, “Bush, Congress Head for Clash Over Ports Deal,” Feb. 22, 2006, stated: “More broadly, a successful move to block the deal could send a chilling signal about some foreign investment in the U.S. at a time when such investment has been critical in sustaining growth.”

the world to invest. So dollars that flow abroad from our purchase of imports are recycled back to us as capital investments.

At the end of 2004 (the most recent figures), foreigners owned about $12 trillion in U.S. assets: $6 trillion in stocks and bonds, $3 trillion in debt to banks and other lenders and $3 trillion in hard assets, like factories. These capital flows employ Americans, raise their paychecks and keep interest rates down.

In recent years, important capital flows are coming from emerging markets, including Asia and the Middle East. These flows are expected to continue – and not just because of oil. As Jeremy Siegel writes, demographic imbalances mean that older people in the U.S. and other developed nations will have to live off the sale of assets to younger people in developing nations.

At any rate, the continuing free flow of capital into the United States is crucial. Dubai has been among the "most prominent recent buyers into the U.S. economy,"[10] with, for example, Dubai International Capital buying a two percent stake in Daimler Chrysler last year.

Now, however, the United States risks developing a reputation as a country that no longer welcomes some people's money. If that happens, other nations – Japan, Britain, Germany, Australia – will attract capital that would have gone to the U.S. The virtuous circle of global trade and investment risks being broken, with disastrous consequences.

That is the real danger here. We shouldn't flatter ourselves. We aren't the center of the world. Look at shipping terminals. The action is not in New York or Los Angeles. It's in Singapore, Hong Kong, and new ports in Shanghai, South Korea and India.

Security

This episode has been a sad one in many ways, but it could help revive interest among policy makers in getting serious about reducing the threat of seaborne weapons of mass destruction. That threat must be attacked at the source. "Our first priority," writes Veronique DeRugy of AEI, "should be to stop terrorists from acquiring fissile material to build a bomb." But just $250 million is spent in these efforts. Our second priority should be to stop such material from getting on ships in foreign ports. DHS's Container Security Initiative, in which the Dubai participates, inspects cargo for WMD before it is shipped. But only $139 million was spent on this program last year. The third priority is security in U.S. ports themselves, where $360 million in spent on in-port detection devices. Far more resources – human, technological and financial – must be devoted to preventing WMD from ever being loaded on a ship.[11]

[10] "Dubai Ports Row Breeds Bad Feeling Among Arab Businesses," Financial Times, Feb. 26, 2006.

[11] As DeRugy writes: "If a nuclear bomb explodes at the port of Philadelphia, it would kill many of the city's 1.5 million residents. It is cold comfort to know the detector's alarm might go off five minutes before you're dead." From "Security Begins Abroad," Wall Street Journal, Feb. 27, 2006.

Would withdrawing the P&O leases from DP World help national security? That's a dubious proposition. It would certainly jeopardize Dubai's role as a loyal American ally – if that role has not been jeopardized already.

Conclusion

Absolutely, keep our ports safe. Trust no one to do that – not the Brits, not the Singaporeans, not the Arabs – but our own law enforcement and military. Their job is to keep the lanes of commerce and communication and travel open, and, so far, they have done a spectacular job. It is now four and a half years since 9/11, and there has not been an attack on U.S. soil. Yes, we can do better, but our efforts should be concentrated abroad.

The United States benefits mightily from a globalized world. Our ties through trade, in fact, have made us more safe as our trading partners become more prosperous, open and democratic. But our politicians and pundits should know that we can't pick and choose. If we decide to deny firms from developing nations – Arab, Asian or otherwise – from investing in the United States, those firms will go elsewhere. And we will pay the price – in higher interest rates, higher mortgage rates, higher inflation, lower stock prices, less participation in a world growing more and more creative and exciting.

Thank you.